No. 12295.

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

NATIONAL BRASS WORKS, INCORPORATED,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

REPLY BRIEF FOR PETITIONER.

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As we understand the Respondent's argument, it may be briefly summarized as follows:

1. Under *Jerry Rossman Corporation v. Commissioner,* 175 F. 2d 711 (C. C. A. 2), a payment to the United States by one who overcharged his customers in violation of the Emergency Price Control Act may be deductible if the violation was not wilful and the seller did not pay more than the overcharge to the United States. But the petitioner here was guilty of a wilful violation and paid more than the precise overcharge to the United States.

2. The *Rossman* case was wrongly decided. Every payment to the United States by an O. P. A. overcharger is necessarily a penalty which cannot be deducted.

A. The Tax Court Failed to Find That the Petitioner's Violations of the Emergency Price Control Act Were Wilful, or That the Petitioner Paid More Than the Face Amount of the Overcharges.

The Respondent's argument depends almost exclusively upon two "facts" which, it is strenuously urged, distinguish this case from *Jerry Rossman Corporation v. Commissioner, supra.* These "facts" are: (1) The petitioner wilfully and deliberately violated the Emergency Price Control Act (Resp. Br. pp. 5, 6, 9, 10, 11, 13, 14, 17, 18, 20, 42, 44, 47); and (2) the petitioner paid more than the face amount of the overcharges to the Office of Price Administration (Resp. Br. pp. 6, 8, 9, 14-15, 21, 34, 42). Indeed the Respondent relies so heavily upon these two "facts," that whenever he ventures a direct attack upon the holding of the *Rossman* case, he is careful to retreat from each attack to the safe harbor which these two "facts" conveniently provide. See Respondent's Brief, pp. 8, 9, 10, 34, 42, 47.

However, as this Court has emphasized time and again, fact finding is exclusively the business of the Tax Court,[1]

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[1]*Helvering v. Rankin,* 295 U. S. 123, 131-132; *Helvering v. Richter,* 312 U. S. 561, 562; *Munter v. Commissioner,* 331 U. S. 210, 216; *Commissioner v. Culbertson,* 337 U. S. 733, 748; *Harbor Plywood Corp. v. Commissioner,* 143 F. 2d 780, 783 (C. C. A. 9); *Belridge Oil Co. v. Helvering,* 69 F. 2d 432, 433 (C. C. A. 9); *Belridge Oil Co. v. Commissioner,* 85 F. 2d 762, 768 (C. C. A. 9); *Anderson v. Commissioner,* 78 F. 2d 636, 637 (C. C. A. 9); *Eaton v. Commissioner,* 81 F. 2d 332 (C. C. A. 9); *Fulton Oil Co. v. Commissioner,* 81 F. 2d 330, 332 (C. C. A. 9); *Dornbecher Mfg. Co. v. Commissioner, supra; Diller v. Commissioner,* 91 F. 2d 194 (C. C. A. 9); *Kelleher v. Commissioner,* 94 F. 2d 294 (C. C. A. 9); *Aronson v. Commissioner,* 98 F. 2d 23 (C. C. A. 9). See also *Bell v. Commissioner,* 139 F. 2d 147, 149 (C. C. A. 3); *Stoddard v. Commissioner,* 141 F. 2d 76, 79 (C. C. A. 2); *Dent v. Alaska Placer Co.,* 177 F. 2d 8 (C. C. A. 9). *Cf. Commissioner v. Boeing,* 106 F. 2d 308-309 (C. C. A. 9).

and the Tax Court has not found the "facts" which are the cornerstone of the Respondent's argument. There is no need to question the license of any advocate, including Government Counsel, to make legal arguments premised on facts which the trial court did not find.[2] For this Court's position on fact finding has been stated with crystal clarity. As this Court said in *Doernbecher Mfg. Co. v. Commissioner,* 80 F. 2d 573 (C. C. A. 9):

> "If the Board has failed to make an essential finding and the record on review is insufficient to provide the basis for a final determination, the proper procedure is to remand the case for further proceedings before the Board. Compare *Helvering v. Taylor,* 293 U. S. 507, 755 S. Ct. 287, 79 L. Ed. 623; *Murphy Oil Co. v. Burnet,* 287 U. S. 299, 308, 53 S. Ct. 161, 77 L. Ed. 318. The same procedure is appropriate even when the findings omitted by the Board might be supplied from examination of the record."

The circumstances of this case graphically illustrate the wisdom of the appellate courts in refusing to make findings of fact. When the Tax Court decided this case, it had already held that *any* payment by an O. P. A. violator

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[2]The Respondent's persistent advocacy well beyond the record reaches a remarkable crescendo when he says:

> "In the instant case, taxpayer during the period of the entire year commencing February 1, 1943, and ending January 31, 1944 [R. 15-16, 81-83], precisely when the war emergency was at its height and the disruptive influences of inflation most serious, committed wilful violations of the maximum prices fixed by law and knowingly entered into a course of conduct which tended to defeat the Congressional objective and the chosen method for achieving that objective, namely, to protect the nation from that inflation, which, as has been seen, the Senate Committee regarded as the most destructive consequence of war except human slaughter. Brief for Respondent, pp. 17-18.

to the Government was a nondeductible penalty. *Scioto Provision Company v. Commissioner,* 9 T. C. 439 (1947); *Jerry Rossman Corporation v. Commissioner,* 10 T. C. 468 (1948).[3] As a result, the "facts" now found in the Respondent's brief were wholly irrelevant. Under the then prevailing theory of the Tax Court it was unnecessary to determine (a) whether the taxpayer paid to O. P. A. the face amount of the overcharges or something more, and (b) whether the taxpayer's violation was deliberate and wilful. Indeed, the Respondent's brief to the Tax Court did not even make an appropriate request that the Tax Court determine these factual questions.

If the "facts" now found by the Respondent are truly relevant, as the Respondent's brief implicitly concedes, the Tax Court necessarily tried and decided the case on the erroneous legal theory that no payments to O. P. A. are deductible, and because of this erroneous theory the Tax Court failed to pass upon the factual issues which the Respondent now apparently considers crucial.

The circumstances of this case clearly require a further hearing in addition to further findings if the case is to be remanded to the Tax Court. The Respondent infers, although the Tax Court made no such finding, that the petitioner settled the Government's treble damage claim by paying treble damages. The Government records are probably the best evidence as to whether the O. P. A. accepted the face amount of the overcharges or exacted an additional sum. Since the trial the Government has indicated that records in its possession show that petitioner paid only the face amount of the overcharges in settle-

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[3]Rev'd 175 F. 2d 711 (C. C. A. 2).

ment of the Government's claim. The Commissioner's brief to the Court of Appeals for the Second Circuit in *Jerry Rossman Corporation v. Commissioner* states:

> ". . . The Tax Court has in four cases denied deductions of payments made to the Price Administrator in compromise of claims for alleged price ceiling violations under Section 205(e). *Scioto Provision Co. v. Commissioner,* 9 T. C. 439; *Garibaldi & Cuneo v. Commissioner,* 9 T. C. 446; *Nazareth Mills, Inc. v. Commissioner,* decided February 16, 1949 . . . ; *National Brass Works v. Commissioner,* decided March 24, 1949 . . . In all these cases the penalty amounted only to the overcharge, except in *Garibaldi & Cuneo v. Commissioner, supra,* where it was one and a half times the overcharge." *Jerry Rossman Corporation v. Commissioner,* Brief for Respondent, pp. 36-37.

This statement by the Commissioner that O. P. A. accepted the face amount of the overcharges in settlement of its claim against National Brass Works is obviously not based upon the Tax Court's findings or the record in this case. It is entirely possible that this fact was gleaned from Government files which showed that in this case O. P. A. accepted simple overcharge payments in settlement of treble damage claims. If so, under the *Rossman* decision the acceptance of the face amount of the overcharge was an administrative determination that the particular violation was neither wilful nor the result of a failure to take practicable precautions. *Jerry Rossman Corporation v. Commissioner,* 175 F. 2d at 714. This administrative determination would rebut the inference which the Respondent has drawn here, contrary to its own brief in the *Rossman* case and without the benefit of a Tax

Court finding, that petitioner wilfully overcharged its customers. Proof that the O. P. A. Administrator accepted the overcharge payment in settlement would bring this case squarely within the orbit of *Jerry Rossman Corporation v. Commissioner,* and pose for the Tax Court the very question which the Respondent seeks to avoid here by arguing outside the record.

It is, of course, possible that on remand the Tax Court may find that the petitioner paid the overcharges plus an additional sum. But even if the petitioner paid an amount in addition to the overcharges, it is still true that at the very least petitioner may deduct the overcharge payments themselves. As the Court of Appeals for the Second Circuit said in the *Rossman* case:

> "(R)ecovery of three times the overcharge is no less a recovery of the overcharge because it includes the penalty along with it. Hence, if the taxpayer had been able to distribute the overcharge to the 'terminal buyers' and had done so, the distribution would have been deductible . . . the Administrator's claim, like the 'terminal buyer's' claim for which it is a substitute, is also made up of the overcharge and an addition of twice its amount . . ." 175 F. 2d at 712.

The Tax Court did not anticipate any distinction between the payment of overcharges and any payment beyond the overcharges. Therefore, a decision on the merits should await a Tax Court finding as to how much, if anything, the petitioner paid in excess of the overcharges it collected from its customers. See *Cohan v. Commissioner,* 39 F. 2d 540 (C. C. A. 2), cited with approval in *Roberts v. Commissioner,* 176 F. 2d 226 (C. C. A. 9). Even if there should be a complete failure of proof on

remand, it is clear as a matter of law that at least one third of the petitioner's payment represented the overcharges and is deductible.

At the very least, therefore, the case must be remanded to the Tax Court for further hearings and findings of fact. *Culbertson v. Commissioner, supra; Fulton Oil Co. v. Commissioner, supra; Kellaher v. Commissioner, supra; Aronson v. Commissioner, supra.*

B. **The Tax Court Erroneously Decided That the Deduction of Overcharge Payments to the United States Would Frustrate a Sharply Defined Public Policy.**

The Respondent seems to recognize that if this Court declines the Respondent's invitation to usurp the fact finding function of the Tax Court, the affirmance of the Tax Court's decision would directly contradict the decision of the Court of Appeals for the Second Circuit in *Jerry Rossman Corporation v. Commissioner.* Accordingly, the Respondent urges that the *Rossman* case was wrongly decided.

The basic legal question in both the *Rossman* case and this case has been framed by the Supreme Court in *Commissioner v. Heiniger,* 320 U. S. 467, 473. The question is whether the allowance of the deduction claimed would "frustrate . . . sharply defined national . . . policies proscribing particular types of conduct." The national policy with regard to those who overcharged in violation of the Emergency Price Control Act was sharply defined by those primarily concerned in articulating and executing that policy—the Congress and the O. P. A. Administrator.

The authoritative Congressional policy reflected by the Price Control Act has been outlined for the Court in a brief filed in this case by Pacific Mills as *amicus curiae*. Brief *amicus curiae* pp. 10-18. Respondent has conspicuously refrained from commenting on the relevant legislative materials as if they did not exist.

We do not wish to burden the Court by reviewing these materials here. They plainly show that in the eyes of Congress the payment of an overcharge was not a penalty, and that the deduction of an overcharge payment would not frustrate any sharply defined public policy.

The Respondent contends that the deduction of overcharge payments would violate a sharply defined public policy because:

1. Some courts in far different contexts have said that overcharge payments to the United States are penalties.
2. The payments must be penalties because they are not restitution.
3. The payments must be penalties because they were collected by the United States to deter violations of the Emergency Price Control Act.

We believe that these arguments are easily answered:

1. The judicial statements upon which the Respondent relies were not at all concerned with the present issue of proper tax incidence. Moreover, the present issue, which turns upon the national price control policy, must necessarily be resolved in the light of that policy as articulated by Congress.

2. The Respondent's argument that overcharge payments must be penalties because the United States did not collect them as restitution is completely question begging. The argument presumes that payments to the Price Administrator must fall into one of two rigid categories: (a) Penalty payments, which are not deductible, and (b) restitution payments, which are deductible.

This arbitrary distinction between restitution and penalty exposes a fundamental fallacy in the Respondent's case. His argument is that any payment to the Government which is not restitution must by sheer definition be a penalty which is not deductible. Needless to say, this argument is an obvious oversimplification. For example, as the *amicus curiae* has pointed out, a farmer pays a "penalty" to the Government if he markets certain products in excess of quotas established by the Government. These payments are not restitution; nevertheless they are deductible. I. T. 3530, C. B. 1942-1, p. 43.

Clearly, under the *Heininger* decision restitution cannot be a test of deductibility. The test is whether the deduction of a particular payment to the Government would frustrate a sharply defined public policy. And the legislative materials rebut the Commissioner's contention that the deduction claimed would frustrate any such policy.

3. Similarly the Respondent is hardly more persuasive when he argues that an overcharge payment to the Government is necessarily a penalty because of its deterrent effect. Any sanction enforced by law has a deterrent effect. For example, the right to recover for a breach of contract or a tort necessarily discourages the commission of a breach or a tort. Yet this Court has held that payments on tort claims are deductible despite their obvious

deterrent effect. *Helvering v. Hampton,* 79 F. 2d 358 (C. C. A. 9.) Furthermore, in the context of the Emergency Price Control Act it is impossible to distinguish, from the seller's point of view, between the deterrent effect of a consumer's right to sue for overcharges and the Administrator's right to do likewise. And, more directly, the Commissioner of Internal Revenue has held that overcharges and damages beyond overcharges paid to the consumer are deductible. I. T. 3627, C. B. 1943, p. 111. In this posture of the law it is difficult for the Commissioner to rely upon the deterrent effect of overcharge payments as the reason for barring their deduction.

In short, the question here, as in the *Rossman* case, is whether the deduction of overcharge payments to the United States would frustrate some sharply defined public policy. We submit that in *Jerry Rossman Corporation v. Commissioner, supra,* the Court of Appeals for the Second Circuit correctly decided that the deduction of overcharges paid to the United States would not frustrate any sharply defined public policy. The Tax Court decision here to the contrary should be reversed and the case remanded for further proceedings and findings.

Respectfully submitted,

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